HOUSING MARKET OUTLOOK

Halifax

Homeownership Market Will Continue to Lose Momentum in 2005-2006

Canada Mortgage and Housing Corporation
www.cmhc.ca

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New Homes Market Outlook

Residential construction activity is expected to slip from last year's level as a rebound in multiple unit construction only partially alleviates a slide in single-detached homebuilding. Total housing starts are forecast to turn in a respectable 2,400 units this year, down nine per cent from 2,627 last year. Although starts are forecast to slip another 3 per cent next year, the anticipated 2,325 total starts will still represent a decent year by historical standards.

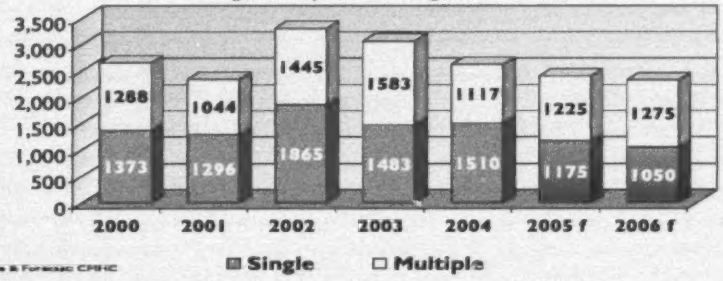
A substantial and fairly rapid expansion in the inventory of existing homes for sale has reduced a key impetus that has been driving the high level of single family homebuilding over the past three years. Through the first quarter of 2005, the number of homes listed for sale through MLS is 21 per cent higher than in the first quarter of last year while single starts are down 15 per cent over the same period. Given the abnormally fair weather in March and April, this decline in starts is certainly not due to weather-related challenges. Furthermore, with a considerably lower level of total housing units under construction across Metro, it is also quite unlikely that the decline in single starts can be attributed to industry capacity constraints such as construction labour or building materials availability. Consequently, an expanding inventory of existing homes for sale must be considered a key contributing factor to the year-to-date decline in single starts.

Since a disproportionately large share of the recent growth in existing home inventory seems to be comprised of relatively expensive homes, homebuilders may be particularly concerned. Over the past two years, much of the demand for 'high-end' single-detached homes has been satisfied by the new construction sector. With a wider selection of existing homes available to potential 'high-end' homebuyers, it will be homebuilders who have targeted the luxury market who will be most affected by changing conditions in the resale market.

This is perhaps why concern is mounting in the industry about an impending oversupply situation in the 'high-end' of the new home market. However, the overall inventory of unsold new single-detached homes remains quite low at only 37 houses in March - enough to last only two weeks at the current level of new home sales. In addition, trends in new home absorption and unsold new home inventory data by price range indicate that there are no serious concerns about an oversupply of unsold *new* single-detached homes at any point in the price spectrum. Nevertheless, the new home market does not operate in isolation from the existing home

Modest declines in total housing starts expected

Single & Multiple Unit Housing Starts, Halifax CMA



Source & Forecast: CMHC

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market; and as more existing homes priced above $250,000 are listed for sale, builders are expected to see fewer potential buyers looking for comparably-priced new homes.

So, with first-time buyers expected to take a larger slice of a shrinking home ownership demand pie, are single-detached homebuilders expected to shift their focus to this segment of the housing market? This is not expected to happen for several reasons. First, construction cost increases in recent years have made it very difficult for builders to produce a new single-detached home of even a modest 1,600 square feet anywhere in Metro for under $225,000. Exacerbating this challenge is a shortage of building lots priced under $60,000, especially in the serviced areas of Metro. Dartmouth, Sackville and Timberlea have been home to much of the relatively affordable new home construction over the past five years, but there are few building lots available in these areas to accommodate such construction activity over the next 18 months. Consequently, the extent to which homebuilders are able to accommodate demand for relatively inexpensive, new single-detached homes over the next two to three years will be largely determined by the rate of growth in supply of relatively inexpensive building lots.

Nevertheless, with aggregate home ownership demand expected to slide over the next 18 months and with the inventory of homes for sale expected to continue to expand, demand for new single-detached homes is forecast to decline irrespective of supply conditions. This trend will result in successive declines in annual single-detached housing starts of 22 per cent this year and 11 per cent in 2006.

Last year total multiple unit housing starts in Metro Halifax dropped 29 per cent from 2003's very high level. A sharp decline in rental housing starts accounted for most of this decline, but lower levels of semi-detached and condominium starts also contributed. Very attractive first-time homeownership conditions deterred some developers from initiating new rental projects, while others exercised more caution in their introduction of new condo projects by requiring the achievement of considerable pre-sale targets before breaking ground.

Condo starts could reach new record levels of 650 units in both 2005 and 2006. Numerous projects are scheduled to break ground before the end of next year, including several very large ones, which will exert tremendous influence on the annual condo starts numbers depending on when their footings are poured. Thus, our condominium starts forecast is the subject of considerable volatility and could change significantly as developments unfold. Expect to see more developers considering relatively inexpensive condo product targeted at first-time buyers since this group is likely to form a growing share of home ownership demand over the next two years. Furthermore, the 'high-end' of the condo market is forecast to tilt in favour of buyers before the end of this year, reducing profitability for new luxury projects.

Although home ownership affordability conditions are expected to gradually worsen over the next two years, mortgage rates will remain quite low through the end of next year, and this will continue to encourage the movement of tenants into home ownership at a steady rate - as long as there is an adequate inventory of relatively affordable housing options. Nevertheless, 2005 is expected to mark the beginning of a five-year tightening phase in the local rental market and commensurately, the beginning of growth in rental construction once again. As the rental vacancy rate begins to shrink, rental housing starts are forecast to increase slightly from 422 units last year to 450 this year and begin to climb at a stronger pace to 500 next year.

High cost structures and equally high buyer and tenant expectations will challenge developers of new rental and condo projects to find ways of producing new units at relatively affordable prices. It is anticipated that this challenge will result in more one-bedroom units in new apartment projects as well as smaller units in square footage terms.

Similar cost challenges have been the driving force behind the rapid growth in the row and townhouse segment of the local new homes market. More builders have been choosing this option as a cost-effective means of delivering good quality new homes to the market at a relatively affordable price, compared with single and semi-detached homes of comparable size. This trend is expected to continue over the next two years as land costs continue to rise and buyers become increasingly price sensitive. As a result, annual declines in row housing starts in 2005 and 2006 are forecast to be much more modest than those for single and semi-detached starts.

In summary, developers and builders will be challenged to produce cost-effective and marketable new homes of all types as consumers become increasingly price-sensitive but maintain their high expectations. This will result in multiple unit starts taking a larger share of total housing starts as well as an increase in new housing product differentiation. However, declining home ownership demand and an expanding inventory of homes for sale will ultimately result in lower levels of total housing starts in both 2005 and 2006.

Economic Outlook

Growth pace to ease

Over the next two years, economic growth in Metro Halifax is expected to be delivered from a strengthening goods sector while the much larger services sector weakens somewhat. As a result, the exceptionally strong 3.9 per cent growth in employment last year is expected to slow to approximately 2.8 per cent this year and to 2.2 per cent in 2006. However, as was the case last year, much of the job growth over the next two years will be full-time and this will provide some support to declining homeownership demand.

The outlook for the non-residential construction sector is particularly optimistic with the $333 million Halifax Harbour Clean-Up project now in full swing, a more than $100 million expansion and improvement of Halifax International Airport facilities continuing, and education facility construction activity poised to remain strong as well. This will be complemented by construction of two new large big box retail parks in Dartmouth (and required highway interchanges) as well as a $45 million Maritime Helicopter Training Centre at CFB Shearwater. As the pace of residential construction slows over the next two years, these projects will be instrumental in supporting continued growth in the construction sector.

Unfortunately, the outlook for the much larger service sector is not quite as rosy. As employment growth slows and inflation creeps upward, annual real personal disposable income gains will shrink over the next two years. In addition, forecast increases in interest and mortgage rates (albeit modest ones) and higher property tax assessments, heating costs, utility and water bills will also lighten consumers' wallets. This will pose a challenge to the retail sales sector to maintain the very strong pace of growth that has been a key pillar of strength for the Metro Halifax economy recently.

High fuel prices are also expected to dampen tourism prospects in 2005 and to a lesser extent in 2006, and this will also adversely impact the trade and transportation sectors as well, although only slightly. Of greater concern is uncertainty about the confidence of Ontario and U.S. consumers and the related impact on the export and tourism sectors of the local economy here.

In summary, the outlook for the local economy could be characterized as good, but not quite as strong as in 2004. In contrast with the past three years, economic growth will increasingly be driven by investment rather than consumption. However, given the much larger size of the local service sector, most of the growth in economic activity and employment will continue to be delivered from this part of the economy.

Resale Market Outlook

Softening trend will continue

Pressure has been easing in the resale market for almost a year now, and this is expected to continue over the next 18 months as the inventory of homes for sale expands impressively and fewer potential buyers enjoy more choice and more time to make a decision. Annual MLS® sales are forecast to decline again in 2005 and in 2006 but these rates of decline will be very modest at two per cent and three per cent, respectively. As market conditions soften, annual rates of price growth are forecast to decelerate to approximately five per cent this year and to just under three per cent in 2006 when average MLS® residential sale price reaches $189,000.

After more than three years of sellers holding the advantage in the local housing market, balanced market conditions finally arrived last fall. Balanced market conditions are expected to persist through the remainder of this year before turning in favour of buyers in the second half of next year as the resale market approaches the trough in the current housing cycle which is expected to occur in 2007.

However, there is considerable upside risk to this forecast. Through the first quarter of 2005 MLS® sales are up 6 per cent compared with the first quarter of last year, while the rate of sale price growth has stabilized at about 6 per cent over the past six months after declining steadily from 10 per cent growth at the beginning of 2004. This suggests the possibility of a higher level of sales occurring this year than in 2004, as well as the potential for a slightly higher rate of price growth, particularly given economic and market conditions that remain very supportive of home ownership demand.

Metro Halifax enjoyed exceptionally strong growth in employment last year with over 7,200 full-time jobs created, an impressive rebound from the moribund labour market performances of 2002 and 2003. Growth in full-time employment typically translates into growth in

home sales over the ensuing 18 months, so it is quite possible that resale market performance this year may reflect the impact of the strong employment growth posted last year.

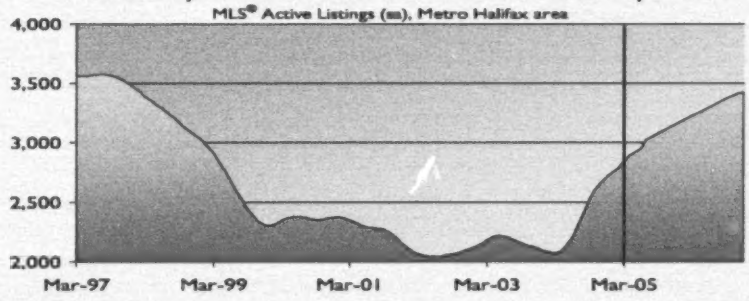
Furthermore, potential buyers have a much better selection of homes to choose from than was true in 2003 and most of 2004. The inventory of homes for sale was 33 per cent higher in March 2005 than the very thin inventory available one year earlier and about 30 per cent higher than what was available in March 2003. In fact, on average through 2003-2004, the level of active MLS® listings was sufficient to satisfy only 4.9 months of sales at any time.

Accordingly, the unexpectedly strong sales activity through the first three months of this year may suggest that there is also some pent-up demand currently being satisfied which accumulated during 2003 and 2004, when sales failed to reach full potential due to an inadequate choice of homes available to potential buyers during that period. However, the aforementioned employment growth, expanding inventory and very low mortgage rates have been factored into our forecasts over the past six months and we do not attribute the strength of resale market activity in the first quarter of this year to these factors. We believe the resale market has simply experienced an early start to the traditional season due to fair spring weather and that this has brought forward a share of sales that would otherwise have occurred in the second quarter.

In summary, home ownership demand conditions are expected to remain very supportive in 2005 and 2006, but this is not expected to reverse the declining trend in the resale market that has been occurring since 2003; it will only mitigate the magnitude of the decline. Mortgage rates are forecast to rise modestly but remain low by historical standards; employment growth will continue but at a more moderate pace, and potential buyers will increasingly enjoy a position of advantage in the market as the inventory of homes for sale expands. However, the stimulative impact of these factors on resale market demand is expected to be somewhat muted due to the fact that so much home ownership demand has already been satisfied over the past three years.

Inventory of homes for sale will continue to expand

MLS® Active Listings (sa), Metro Halifax area



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Source: CREA & NSAR

Seasonal Adjustment (sa): CMHC

Rental Market Outlook

Tightening Phase Ahead

Rental market conditions in Metro Halifax relaxed last year after a six-year tightening trend. The rental apartment vacancy rate increased to 2.9 per cent from 2.3 per cent in 2003 but the market remained in a balanced condition overall. This increase in vacancy rate can be attributed to two key factors: The substantial increase in new supply of rental units with the addition of 877 apartments to the market; and, the adverse impact on rental demand of last year's very magnetic homeownership conditions.

Although mortgage rates remain very low, 'affordable' housing options for potential first-time buyers are becoming more limited and this is stemming the flow of tenants to home ownership. With the annual rate of house price growth expected to at least match real personal disposable income growth over the next 18 months, this situation is expected to persist through the end of next year. In addition, mortgage rates are forecast to begin to climb later this year and this will continue through next year, although increases will be limited to only about 100 basis points in total. Nevertheless, this will also have a dampening impact on home ownership affordability which will be exacerbated by rising heating costs, property tax assessments, utility rates and water bills. Monthly home ownership carrying costs in Metro Halifax for someone purchasing a new home at the average MLS® price are expected to be approximately 15 per cent higher in December 2006 than they were in March of 2005. This worsening in home ownership affordability conditions is the key factor behind what is expected to be a slight increase in rental demand this year and a more significant increase next year.

Exceptionally attractive home ownership conditions have also influenced developers to start fewer new rental projects over the past two years and this will result in rental completions

returning to more typical levels of 575 in the 2005 CMHC Rental Market Survey year (July 1st – June 30th) and 660 in 2006. Consequently, growth in rental demand is forecast to outpace growth in new supply of apartments, pulling down the vacancy rate to 2.7% this year and down again to 2.3% in 2006. With tightening rental market conditions and worsening home ownership affordability conditions, landlords will have the latitude to raise rents to recoup higher operating costs on items such as heat, utilities, water and advertising as was the case in 2004. As a result, average monthly rent in Metro is expected to rise 3-4% to $730 per month this year and another 4-5% next year reaching $765.

Renovation Market Outlook

2005 will be another great year
The results of the latest CMHC Consumer Intentions to Buy or Renovate a Home (ITBR) show that among the six major markets surveyed across Canada (Vancouver, Calgary, Toronto, Ottawa, Montréal, Halifax), intentions to renovate are highest in Metro Halifax. Forty-five per cent of households in Metro Halifax indicated that they intend to renovate their home between the fourth quarter of 2004 and the fourth quarter of 2005. In fact, more than one-third of homeowners in Halifax are "ready to renovate"; that is, they have indicated that there is a high chance that they will renovate their home within the next 12 months and that the total cost of renovations will be $1,000 or more.

Comparing the 2004 ITBR survey results to those of the 1999 Survey shows that intentions to renovate have increased substantially over the last five years. The 1999 Survey found that 19 per cent of homeowners in Halifax were "ready to renovate" compared with 35 per cent in 2004. This significant increase in local renovation intentions has occurred in concert with strong growth in the home ownership market and the two are closely related. As more households purchased homes, many subsequently decided to renovate them to better suit their needs and desires. In addition, a thin inventory of homes for sale in the 2002-2004 period encouraged some homeowners to renovate their existing home rather than buy one, while it also resulted in a larger share of buyers settling for a home that wasn't 'perfect', with the full intention of renovating it soon after to better suit their preferences. Supporting all of this purchase and renovation activity was the exceptionally strong growth in home values which provided homeowners with equity to finance their renovations, and also encouraged investment in housing rather than alternative sources which were not performing nearly as well.

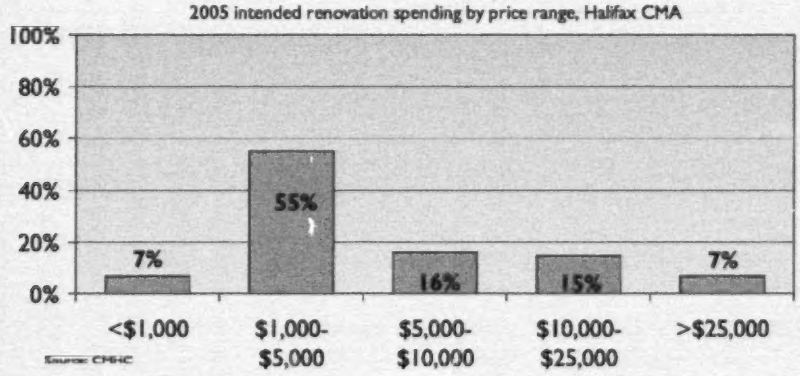
The types and scale of renovation projects Metro Halifax homeowners intend to pursue have also changed over the past five years. In 1999, upgrading the paint/wallpaper in more than one room of the house was the most popular renovation project, while in 2004 more households expressed plans to replace windows and doors (20%) and replace carpet or flooring in more than one room (19%). Intentions for major kitchen upgrades were also more popular in 2004 with 10 per cent of homeowners planning to renovate the hub of their home, compared with 4 per cent in 1999.

The average amount that Metro Halifax homeowners intend to spend on their renovation projects this year is $8,937, compared with $5,287 five years ago, as a larger share of households are planning more expensive renovations. Compared with five years ago, the proportion of households planning to spend between $5,000 and $10,000 on their renovation projects increased six per cent, while those intending to spend more than $10,000 increased 15 per cent.

In summary, 2005 is expected to be another excellent year for renovation activity in Metro Halifax. In fact, the renovation sector is poised to be the strongest among all sectors of the local housing market this year and again in 2006.

Over half of reno intenders will spend $1,000 to $5,000

2005 intended renovation spending by price range, Halifax CMA



Source: CMHC

FORECAST SUMMARY

Metro Halifax- October 2004

	2003	2004	2005 F	% change	2006 F	% change
RESALE MARKET						
MLS® Active Listings (June peak)	2460	2338	2950	26.2%	3300	11.9%
Residential MLS® Sales	5813	5516	5400	-2.1%	5250	-2.8%
Residential MLS® Average Price	$ 162,486	$ 175,132	$ 184,000	5.1%	$ 189,000	2.7%
NEW HOME MARKET						
Total Starts	3066	2627	2400	-8.6%	2325	-3.1%
Single-detached	1483	1510	1175	-22.2%	1050	-10.6%
Multiple Unit	1583	1117	1225	9.7%	1275	4.1%
Semi-detached	227	142	125	-12.0%	100	-20.0%
Row	184	166	150	-9.6%	125	-16.7%
Apartment	1172	809	950	17.4%	1050	10.5%
Condominium (all structure types)	530	401	525	30.9%	525	0.0%
Average New House Price (Single-detached)	$ 211,739	$ 233,914	$ 240,000	2.6%	$ 244,000	1.7%
RENTAL MARKET						
Vacancy Rate	2.3%	2.9%	2.7%		2.3%	
Average Rent-	$675	$705	$735	4.3%	$775	5.4%
Rental Housing Starts	713	422	450	6.6%	500	11.1%
ECONOMIC OVERVIEW						
Mortgage Rate- 3 year term	5.82%	5.65%	5.87%		6.37%	
Mortgage Rate- 5 year term	6.39%	6.23%	6.32%		6.83%	
Employed	195,208	202,821	208,500		213,087	
Employment growth	2.3%	3.9%	2.8%		2.2%	
Unemployment rate	6.8%	6.1%	5.9%		5.7%	

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Source: CMHC

Statistics Canada: Labour Force Survey

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For more information, or to subscribe, contact Michele Clark, Market Research & Client Service Specialist at the Atlantic Business Centre at (902) 426-4708. Order no. *7365E*

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